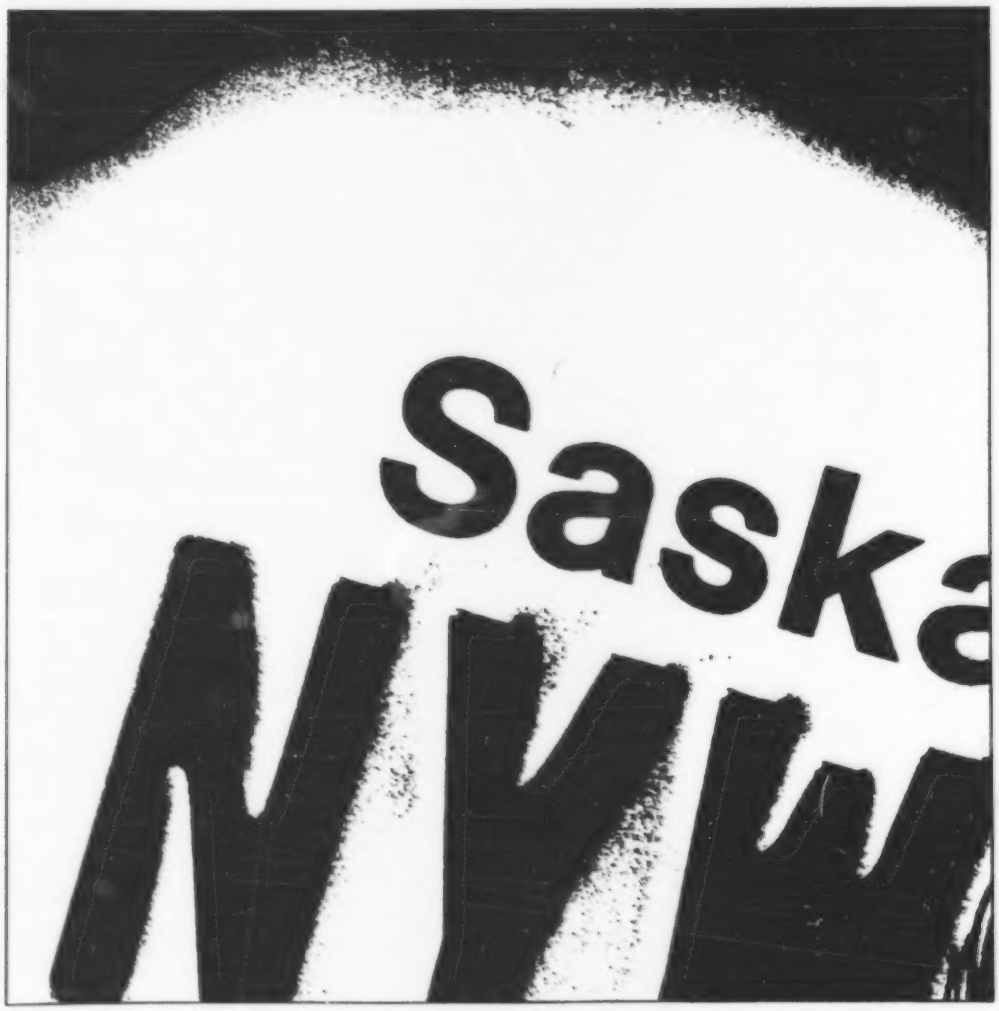
SASKATCHEWAN AUTO FUND

1987 Annual Report



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Yorkton

Mr. Ed Sulewski
Paddockwood

Executive

Standing Left to Right: Alan Cockman, Vice-President, Systems; L. Jill Hilsden, Vice-President, Finance; Grant Gibson, Vice-President, Motor Vehicle Division. Sitting Left to Right: Margo Fries, Assistant to the President and Secretary to the Board; Alex Wilde, President; Larry Fogg, Vice-President, Claims, and Bob Warren, Vice-President, Underwriting Operations.

Letter of Transmittal

Regina, Saskatchewan
March, 1988

To His Honour,
The Honourable F. W. Johnson,
Lieutenant-Governor of the Province of Saskatchewan

Sir:

I have the honour to submit herewith the annual report of the Saskatchewan Auto Fund for the year ended December 31, 1987, including the financial statements in the form required by the Treasury Board and in accordance with the Automobile Accident Insurance Act.

I have the honour to be, Sir,

Your obedient Servant,

Graham Taylor

Graham Taylor
Minister in Charge of
Saskatchewan Auto Fund

President's Message

1987 was a difficult year for the insurance industry, as injury and liability claims costs rose dramatically. The Saskatchewan Auto Fund is not immune to this continuing trend.

Our operating results reflect the 32 per cent jump in bodily injury and liability claims costs we experienced. The Fund recorded a loss of $28.7 million, bringing the Rate Stabilization Reserve to $3.1 million by year-end.

Despite this, the Auto Fund enjoyed many successes. Among many other service achievements, we supported and promoted programs aimed at enhancing safety for motorists throughout the province. This activity demonstrates our commitment to protecting Saskatchewan's residents, not only by offering them basic, comprehensive insurance protection, but by providing them with the means and information to limit or avoid accidents.

Alex Wilde

Alex Wilde
President

The Year in Review

Since 1946, the Auto Fund has provided Saskatchewan drivers with affordable, basic auto insurance.

History of the Auto Fund

In April 1946, the Saskatchewan government passed the Automobile Accident Insurance Act (AAIA) to provide automatic insurance coverage with the purchase of a driver's licence and vehicle registration.

Considered a utility, the Auto Fund is not profit-oriented; rather, it operates on a break-even basis over time. The financial performance of the Fund depends primarily on the cost of collision, injury and liability claims. As claims fluctuate, some years result in a surplus, others result in a deficit. Surpluses and deficits are recorded in the Rate Stabilization Reserve. A strong Rate Stabilization Reserve is important, because it helps keep rates stable for motorists during years of high claims costs to the Fund.

1987: A Financial Overview

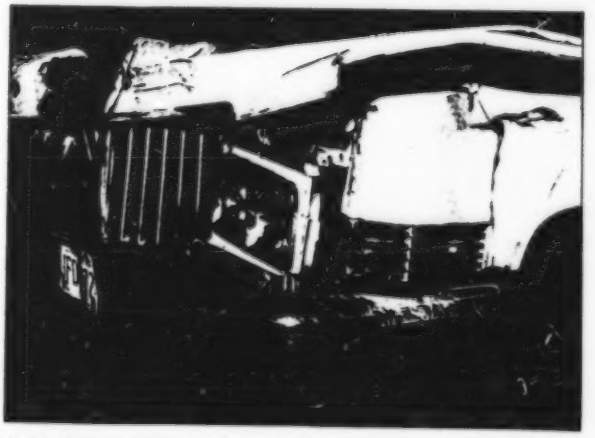
The Saskatchewan Auto Fund ended 1987 with a loss of $28.7 million, compared to a $6.1 million loss in 1986. At year-end 1987, the Rate Stabilization Reserve was reduced to $3.1 million. Claims incurred rose 16 per cent, while total revenue for 1987 increased only 4 per cent over 1986.

The Saskatchewan Auto Fund promotes safer driving conditions with programs like Lights on for Life, which encourages motorists to use their headlights at all times.

Injury and Liability Claims Escalate

Bodily injury and liability claims costs rose from $74.8 million in 1986 to $99.1 million in 1987, a staggering 32 per cent increase. Changes in public attitudes and the legal environment are largely responsible for this dramatic rise.

The vast majority of the rise in liability claims costs is compensation for non-economic ("pain and suffering") losses associated



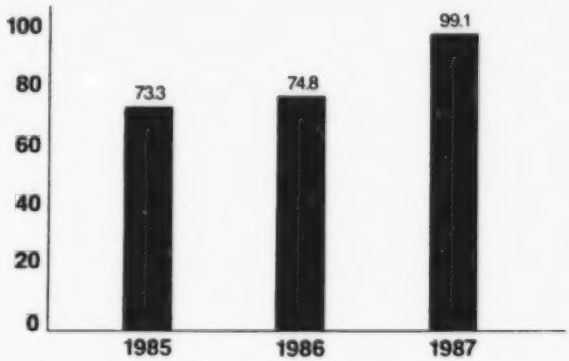
Auto damage claims costs rose 6% in 1987, from $123.8 million to $130.8 million.

with relatively common injuries, like whiplash. In the past, people were not demanding compensation for these types of injuries as frequently as today.

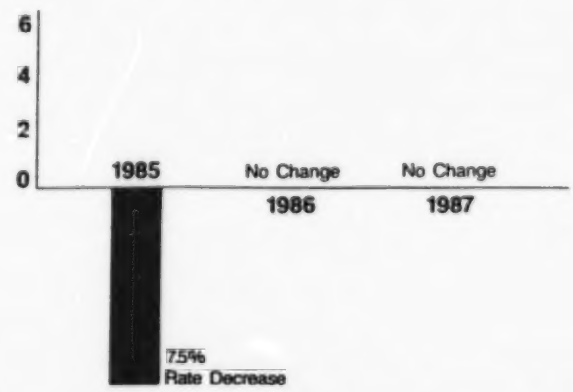
Department interaction promotes growth: Glen Samuelson, Manager of Driver Development, discusses project with Research Officer Glen Parker.

More frequent and higher court awards are part of the picture. Public awareness of liability coverage has risen, and more people are suing one another than previously. In recent years, it has also become easier for passengers to sue drivers for damages. For example, since 1985, spouses have been able to sue one another for damages arising from a motor vehicle accident. Changes to prejudgement interest laws mean that interest paid on court settlements accrues earlier, also driving costs up. These costs have had a dramatic impact on the Fund in recent years.

3-Year Comparison
Bodily Injury & Liability Claims Costs
$(Millions)



3-Year Comparison
Rate Changes



Revenue Base

Auto Fund rates have not increased since 1983, when rates rose 3 per cent. In fact, rates dropped significantly in 1985, meaning that the Auto Fund has operated with a reduced revenue base for some time. In 1985, the Public Utilities Review Commission (PURC) ordered a 7.5 per cent rate reduction, a $15 reduction on driver's licences, along with the good driver bonus program, which alone returned approximately $20 million to drivers with good driving records.

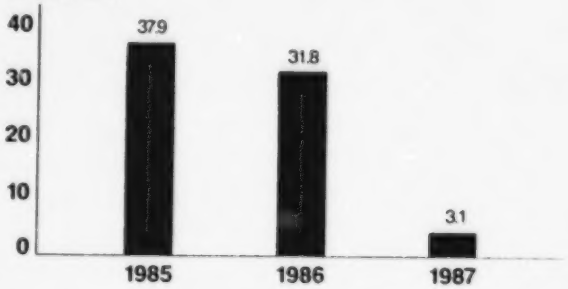
In 1987, a plan for an average 10 per cent vehicle rate increase for 1988 was accepted, to bolster the Fund's sagging financial situation.

Rating

Vehicle rates are primarily based on the repair costs of each vehicle make and model, plus an assessment

for the cost of injury and liability coverage. The purchase price of a vehicle is not as important as repair costs when setting rates, because most vehicles are repaired, not paid out for value.

3-Year Comparison
Rate Stabilization Reserve
$ (Millions)



Drivers found to be at fault in an accident, or those with more than one traffic conviction, are assessed a surcharge on their driver's licence, because of the higher risk they present. This additional premium helps keep vehicle rates as low as possible for good drivers.

Safety Programs Work

The Saskatchewan Auto Fund had a long history of involvement with traffic safety programs, and we are strongly committed to even greater participation in the future. Lower insurance costs are only part of the picture – safety programs save lives and reduce the terrible human tragedy of traffic accidents.

Paul Landry and Bob Lamble are part of the team that develops traffic safety programs for Saskatchewan residents.

Traffic Safety Services

Since July, 1986, the Auto Fund oversees driver testing and development, research, vehicle inspections, and traffic safety programming.

For example, approximately 20,000 vehicles were inspected last year, ranging from power units and semi-trailers to school and passenger buses. In conjunction with Transport Canada, the Auto Fund also conducted an important survey of nighttime drivers, in an effort to assess the extent of nighttime drinking and driving.

Marvin Skalicky carries out a vision test. Twenty-one thousand were performed in 1987.

Staff at our 12 driver testing offices throughout the province processed approximately 67,000 written tests, 21,000 vision tests, 32,000 road tests, booked 77,000 appointments and travelled half a million kilometers.

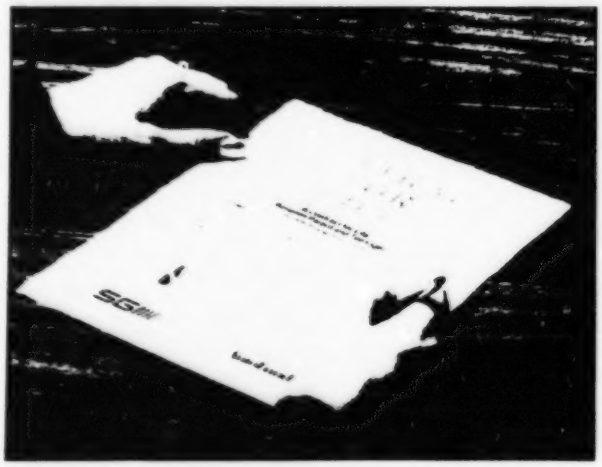
In 1987, approximately 2,500 people took part in Driving Without Impairment, an educational course developed by the Department of Education and sponsored by the Auto Fund. The course educates people convicted of impaired driving about the legal and social issues surrounding drinking and driving, in an effort to avoid repeat offenses.

Seatbelts Save Lives

Research shows that if you're involved in an accident, your chances of being injured or killed are reduced by half if you wear a seatbelt or lapbelt. Determined to do our part in reducing injuries and fatalities, the Auto Fund in 1987 urged the RCMP and city police forces to step up enforcement of the province's seatbelt laws. Saskatchewan motorists responded impressively: in just 5 short months, usage jumped 12 per cent province-wide. During the same 5 months, fatalities on Saskatchewan highways dropped 14 per cent, a promising sign.

Statistics show that buckling up can reduce injuries and fatalities by 50 per cent.

Our commitment to this effort is growing. In 1987, Auto Fund staff worked with other government departments and the Saskatchewan Safety Council to develop an aggressive seat belt program to be launched in 1988. The program will include advertising, seminars with police departments, enforcement efforts, and rental programs for child restraint systems.



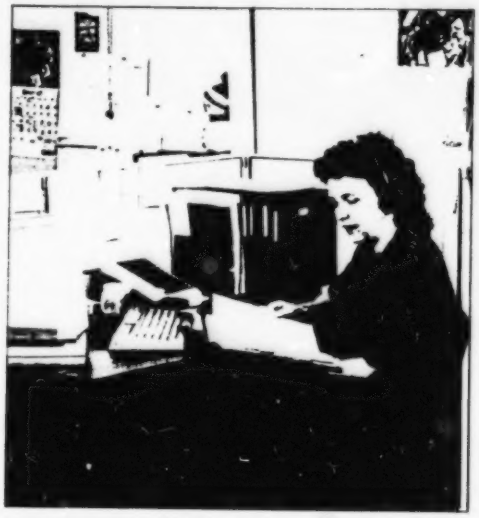
The SADD contract: students and parents join forces to fight drinking and driving.

SADD

In 1987, the Auto Fund worked hand-in-hand with the Saskatchewan Safety Council to promote Students Against Driving Drunk (SADD) to our province's youth. The Auto Fund's 1987 grant of $70,000 paved the way for this important program, which educates young adults about the risks involved with drinking and driving, improves their knowledge and attitudes about alcohol and, most importantly, saves lives.

The success of SADD is remarkable. The Safety Council has made great strides with the program in a very short time: 35 schools in Saskatchewan have established SADD chapters and the Council has hosted four Regional Conferences, attended by approximately 750 students and teachers from 78 schools.

Amelia Krienke and Pat Gouk process vehicle registrations for customers Emmo Janssen, Ken White and Lauri Sawchuk.



Approximately 500,000 calls are handled yearly by Inquiry Centre staff like Licence Clerk Darla Schmidt.

Auto Fund Staff – Keen on Service

Our employees work hard to give the public the high quality service it deserves. To help employees develop their customer service skills, we have developed special in-house training sessions that focus on the importance of fast, courteous and reliable public service. Our reputation for fast, professional claims service reflects our success.

Working at peak efficiency is a goal every business tries to achieve. One example of this is our Inquiry Line, where our staff help half a million callers each year with information about rates, registration, licence suspensions and other procedures. Remarkably, this large workload was handled by fewer staff in 1987 than in 1986. This required a 40 per cent increase in productivity per person, a credit to our hardworking staff.

Responsibility for Financial Statements

The financial statements of the Saskatchewan Auto Fund have been prepared by the management of Saskatchewan Government Insurance as administrator of the Fund in conformity with accounting principles generally accepted in Canada. The financial statements have been examined and approved by the Board of Directors of Saskatchewan Government Insurance. The independent auditors have performed an audit of the Fund which has enabled them to express their opinion on the financial statements of the Saskatchewan Auto Fund. This opinion is shown on page 10.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of the Saskatchewan Auto Fund. Management maintains an extensive system of internal accounting controls to ensure that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements. The adequacy and operation of the control systems are monitored on an ongoing basis by an internal audit department.

An Audit Committee, composed of members of the Board of Directors of Saskatchewan Government Insurance, administrator of the Fund, meets periodically with financial officers of the corporation and the external auditors. The independent auditors have free access to this Committee, without management present, to discuss the results of their audit work and their opinion on the adequacy of internal financial controls and the quality of financial reporting.

L. Jill Hilsden

L. Jill Hilsden
Vice-President
Finance
Saskatchewan Government Insurance
as Administrator of the Saskatchewan Auto Fund

Auditors' Report

February 26, 1988

To the Members of the Legislative Assembly
Province of Saskatchewan:

We have examined the statement of financial position of the Saskatchewan Auto Fund as at December 31, 1987, and the statements of operations and rate stabilization reserve and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the Fund as at December 31, 1987, and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied after giving retroactive effect to the changes in accounting policies as explained in note 2 to the financial statements, on a basis consistent with that of the preceding year.

The financial statements of the previous year were examined by another auditor.

Coopers & Lybrand

Chartered Accountants

Statement of Financial Position

December 31	1987	1986
	(Thousands of $)	
Assets		
Cash and Investments Maturing Within One Year	$ 50,813	$ 70,950
Accounts Receivable	12,862	12,018
Deferred Policy Acquisition Costs	5,241	5,057
Prepaid Expenses and Inventories	1,482	1,544
Long-Term Investments (Note 4)	226,617	191,094
Net Investment in Capital Lease (Note 5)	8,949	9,041
Property, Plant and Equipment (Note 6)	21,267	20,322
	$327,231	$310,026
Liabilities		
Accounts Payable and Accrued Charges	$ 5,085	$ 4,645
Premium Taxes Payable	8,109	7,674
Provision for Unpaid Claims (Note 7)	215,111	172,833
Unearned Premiums	95,849	93,082
	324,154	278,234
Rate Stabilization Reserve	3,077	31,792
	$327,231	$310,026

(See accompanying notes)

Statement of Operations & Rate Stabilization Reserve

Year Ended December 31	1987	1986
	(Thousands of $)	
Premiums Written	$202,369	$191,425
Premiums Earned	$198,812	$190,274
Investment Earnings (Note 8)	34,939	34,474
Other Income (Note 9)	2,031	1,525
Total Revenue	**235,782**	226,273
Claims Incurred	229,838	198,626
Issuer Fees	4,034	3,752
Premium Taxes	7,968	7,627
Administrative Expenses	22,657	22,412
Total Claims and Expenses	**264,497**	232,417
Net Decrease to Rate Stabilization Reserve	**(28,715)**	(6,144)
Rate Stabilization Reserve:		
Balance Beginning of Year		
As Previously Reported	38,843	45,827
Effect of Changes in Accounting Policies (Note 2)	(7,051)	(7,891)
As Restated	31,792	37,936
Balance End of Year	**$ 3,077**	$ 31,792

(See accompanying notes)

Statement of Changes in Financial Position

Year Ended December 31	1987	1986
	(Thousands of $)	
Operating Activities		
Net Decrease to Rate Stabilization Reserve	$(28,715)	$ (6,144)
Items not Affecting Cash:		
Depreciation and Amortization	1,225	797
Realized Gains on Disposal of Investments and Fixed Assets	(6,982)	(6,024)
	(34,472)	(11,371)
Increase in Deferred Policy Acquisition Costs	(184)	(169)
Increase in Accounts Receivable	(844)	(3,102)
Decrease in Prepaid Expenses and Inventories	62	938
Increase in Provision for Unpaid Claims	42,278	27,613
Increase in Unearned Premiums	2,767	2,274
Increase (Decrease) in Accounts Payable and Accrued Charges	440	(2,265)
Increase in Premium Taxes Payable	435	901
Cash Provided by Operating Activities	**10,482**	14,819
Investing Activities		
Long-Term Investments — Purchases	(152,818)	(134,593)
— Proceeds on sale	124,385	117,526
Capital Lease Repayment	92	84
Fixed Assets — Purchases	(2,513)	(6,436)
— Proceeds on disposal	235	47
Net Investing Activities	**(30,619)**	(23,372)
Decrease in Cash and Investments Maturing Within One Year	**(20,137)**	(8,553)
Cash and Investments Maturing Within One Year:		
Balance Beginning of Year	70,950	79,503
Balance End of Year	**$ 50,813**	$ 70,950

(See accompanying notes)

Notes to the Financial Statements

1. Significant Accounting Policies

The Fund's accounting policies are in accordance with generally accepted accounting principles. The following are considered to be significant:

Premiums

Premiums written are taken into income over the terms of the related policies. Premiums not yet taken into income represent the portion of the policy premiums relating to the unexpired term of each policy.

Deferred Policy Acquisition Costs

Premium taxes and issuer fees are deferred and then charged to expense over the terms of the insurance policies to which such costs relate.

Investments

Bonds, debentures and mortgages are recorded at amortized cost. Shares are recorded at cost.

Investment Earnings

Interest is recorded as income on the accrual basis. Dividends are recorded as income on the record date. Gains and losses realized on the disposal of investments are recognized in income on the date of sale.

Provision for Unpaid Claims

The provision for unpaid claims includes the estimated cost to the Fund of reported claims, an estimate based on the claims settlement experience of the Fund of the cost of claims yet to be reported and an estimate of adjustment expenses to be incurred on the settlement of these claims.

Long-term disability claims are recorded on a discounted basis to take account of the time value of money.

Capital Lease

Investment earnings related to the direct financing lease are recognized in a manner that produces a constant rate of return on the investment in the lease. The net investment in the lease is composed of net minimum lease payments less unearned finance income.

Property, Plant and Equipment

Fixed assets are recorded at cost less accumulated depreciation. Depreciation is recorded on a straight-line basis, commencing in the year in which the assets are placed in service, over the estimated useful lives of the fixed assets as follows:

Buildings	2½ – 10%
Furniture and Equipment	20%

Foreign Currency Translation

Share investments, revenues and expenses are translated at the exchange rate in effect at the transaction date.

Administrative Expenses

Saskatchewan Government Insurance (SGI) as administrator of the Saskatchewan Auto Fund incurs certain administrative expenses which cannot be readily or economically identified with the operations of SGI or the Saskatchewan Auto Fund. Section 97 of the Automobile Accident Insurance Act provides that the Board of Directors of SGI may make rules for the allocation of these expenses between SGI and the Auto Fund. These administrative expenses are shared equally as approved by the Board of Directors. This treatment is consistent with the allocation used in the prior year.

Identifiable administrative expenses are charged directly to the Fund's operations.

2. Changes in Accounting Policies

In 1987, the Fund changed its accounting policies to conform to recent changes in industry accounting practices. Comparative figures in these financial statements have been restated to reflect retroactive application of these policies. The effects of the changes are as follows:

(1) Investments

The Fund has changed its accounting policy for shares and convertible bonds from the five-year moving average market valuation method to the cost basis. The accounting policy for gains and losses on disposal of bonds, debentures and mortgages has been changed from the deferral and amortization method to the immediate income recognition method.

The effect of this change has been to decrease the assets and Rate Stabilization Reserve of the Fund by $407,000 as at December 31, 1985. Assets have been increased by $1,333,000 as at December 31, 1986. Investment earnings and consequently the Rate Stabilization Reserve for 1986 and 1987 have increased by $1,740,000 and $2,044,000 respectively.

(2) Provision for Unpaid Claims

The Fund has adopted the practice of estimating future internal loss adjustment expenses on unpaid and unreported claims and including this estimate in the liability for unpaid claims.

The effect of this change has been to increase the liabilities of the Fund and consequently decrease the Rate Stabilization Reserve by $7,484,000 as at December 31, 1985. The liabilities of the Fund have been increased by $8,384,000 as at December 31, 1986. Claims incurred increased and the Rate Stabilization Reserve decreased by $900,000 for 1986 and $1,161,000 for 1987.

The net effect of these changes in accounting policies has been to reduce the Rate Stabilization Reserve by $7,891,000 as at December 31, 1985 and reduce the net decrease to the Rate Stabilization Reserve by $840,000 and $883,000 for 1986 and 1987 respectively.

3. Status of the Fund

The Saskatchewan Auto Fund was established effective January 1, 1984 by an amendment to the Automobile Accident Insurance Act (Chapter A-35, Revised Statutes of Saskatchewan 1978).

The accumulated earnings of the Saskatchewan Auto Fund in the Rate Stabilization Reserve are for the future benefit of Saskatchewan's motoring public and cannot be used for the payment of general dividends.

4. Long-Term Investments

The components of the Fund's long-term investments are as follows:

(Thousands of $)

	1987		1986	
	Book Value	Market Value	Book Value	Market Value
Bonds and Debentures	$ 169,828	$ 170,631	$ 137,235	$ 149,676
Mortgages	14,884	15,150	15,990	16,702
Shares and Convertible Bonds	41,905	38,394	37,869	40,127
Total Long-Term Investments	$ 226,617	$ 224,175	$ 191,094	$ 206,505

5. Net Investment in Capital Lease

The Fund, as lessor, has a 63 per cent interest in a lease agreement with a Government department for a term of thirty years (twenty-three years remaining) on property in Prince Albert. The lease transferred substantially all of the benefits and risks incident with the ownership of the property to the lessee.

The Fund's net investment in capital lease includes the following:

(Thousands of $)

	1987	1986
Total minimum lease payments receivable ($995,000 per year)	$ 23,128	$ 24,123
Unearned income	(14,179)	(15,082)
Net Investment in Capital Lease	$ 8,949	$ 9,041

6. Property, Plant and Equipment

The components of the Fund's investment in property, plant and equipment, as well as the related accumulated depreciation, are as follows:

	(Thousands of $)			
	1987			1986
	Cost	Accum. Depr.	Net Book Value	Net Book Value
Land and Improvements	$ 3,120	$ –	$ 3,120	$ 3,045
Buildings	18,809	3,585	15,224	14,480
Furniture and Equipment	6,113	3,190	2,923	2,797
Total	$ 28,042	$ 6,775	$ 21,267	$ 20,322

7. Discounted Claims Reserves

Included in the provision for unpaid claims are discounted reserves for long-term disability claims in the amount of $11,358,000 (1986 – $11,971,000). These reserves have been discounted at 7% (1986 – 6%) to take account of the time value of money.

8. Investment Earnings

The components of investment earnings are as follows:

	(Thousands of $)	
	1987	1986
Interest and Dividends	$ 27,221	$ 27,545
Realized Gains on Sale of Investments	6,815	6,018
Income from Capital Lease	903	911
Total Investment Earnings	$ 34,939	$ 34,474

9. Salvage Division

The Fund operates a Salvage Division in order to maximize the derived economic value of salvageable vehicles, vehicle parts and materials available through the claims settlement process. In 1987, total salvage sales were $12,899,000 (1986 – $11,835,000); gross earnings on sales were $4,400,000 (1986 – $4,131,000); and net earnings were $1,890,000 (1986 – $1,525,000). The net earnings of the Salvage Division are included in other income.

10. Related-Party Transactions

Included in these financial statements are income and expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan Crown-controlled departments, agencies and corporations with which the Fund is related.

Account balances resulting from these transactions are included in the Statement of Financial Position, and are settled on normal trade terms.

11. Comparative Financial Information

For comparative purposes, certain 1986 balances have been reclassified to conform with the 1987 financial statement presentation.